

June 1, 1998

**CERTIFIED MAIL,
RETURN RECEIPT REQUESTED**

Mr. R. J. Buraglio
Lockheed Martin Advanced
Environmental Systems, Inc.
1920 E. 17th Street, Suite 103
Idaho Falls, Idaho 83404

LOCKHEED MARTIN IDAHO TECHNOLOGIES COMPANY (LMITCO) SUBCONTRACT
NO. C91-133136 - TERMINATION - GHL-031-98

Dear Mr. Buraglio:

Pursuant to the Termination for Default clauses in the subcontract (Clause 53, "Termination for Default (Revised)" of the EG&G Idaho, Inc. Standard Terms and Conditions for Purchase Orders and Subcontracts, Revised for Pit 9; June 1994, and Clause 6, "Termination for Default--Damages for Delay--Time Extensions" of the EG&G Idaho, Inc. Construction Subcontract General Provisions, Revised for Pit 9; June 1994), LMITCO¹ hereby terminates Subcontract No. C91-133136 for default.

By correspondence dated February 27, 1998 (GHL-013-98), LMITCO notified Lockheed Martin Advanced Environmental Systems, Inc. (LMAES)² that LMITCO had determined conditions existed pertinent to the performance of Subcontract No. C91-133136 which necessitated issuance of a cure notice. The aforementioned cure notice requested that, within 30 calendar days after receipt of the notice, LMAES provide adequate assurances demonstrating how LMAES intended to fulfill its contractual obligations to remediate Pit 9. LMITCO defined adequate assurances as ". . . a definitive plan (and demonstrable actions towards implementing that plan) for LMAES fulfilling its obligations under the subcontract." The cure notice stated explicitly that LMAES' failure to provide adequate assurances of performance could constitute the basis for LMITCO to terminate the referenced subcontract for default.

¹ For ease of reference, LMITCO will be used herein to refer to both LMITCO and LITCO (Lockheed Idaho Technologies Company.)

² For ease of reference, LMAES will be used herein to refer to both LESAT (Lockheed Environmental Systems and Technologies Co.) and AWC-Lockheed.

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LMAES responded on April 13, 1998, after having requested and received a two-week extension of time. LMAES' response consisted of the following: (1) a forwarding letter, 8 pages in length; (2) a "detailed response" consisting of 77 pages; and (3) 8 volumes of "reference documents" which contained copies of various documents that were referenced in the detailed response.

Apart from the response to the cure notice, on March 6, 1998, the President and Chief Operating Officer of the Lockheed Martin Energy and Environmental Sector, of which LMAES is a part, wrote to the Manager of the Idaho Operations Office of the United States Department of Energy and advised the Department of Energy-Idaho Operations Office (DOE-ID) of Lockheed Martin Corporation's (LMC) position that "Lockheed Martin is not required to continue to attempt to remediate Pit 9," and further stated ". . . LMAES' obligation to perform the Pit 9 subcontract terminated on September 13, 1997, notwithstanding LMITCO's attempt to extend the contract schedule unilaterally." LMC, in additional correspondence to DOE dated April 14, 1998, did not modify or alter that position.

LMITCO has carefully considered LMAES' response to the cure notice, together with LMC's correspondence of March 6, 1998, and April 14, 1998. While LMAES' response to the cure notice asserted a number of excuses for nonperformance, conspicuous by its absence was ". . . a definitive plan (and demonstrable actions towards implementing that plan) for LMAES fulfilling its obligations under the subcontract." Accordingly, by this letter and in accordance with the terms of the subcontract and applicable law, LMITCO hereby terminates Subcontract No. C91-133136. The basis for this termination is that LMAES has refused and failed to make progress so as to endanger performance of the subcontract, and LMAES has failed adequately to cure its default after proper notice. In addition, LMC's correspondence of March 6, 1998, and LMAES' response to the cure notice constitute clear and unequivocal repudiation of LMAES' contractual obligations. This repudiation constitutes a separate and independent basis for this termination action.

While not required to do so, LMITCO feels it appropriate to address some of the legal arguments made in LMAES' response to the cure notice, as well as the aforementioned March 6, 1998, correspondence from LMC. LMITCO does not believe that this is the time for a point-by-point refutation of the arguments and statements made in LMAES' April 13, 1998, response, many of which appear factually inaccurate or distorted. Any failure in this letter to address any particular statement in LMAES' response or LMC's correspondence should not be construed as LMITCO's agreement with any such statement or assertion.

This response is divided into four parts: (1) a brief history of this procurement; (2) a brief

summary of the project and the reasons why LMITCO concluded that LMAES has failed or refused to make progress and repudiated the subcontract; (3) a brief response to one of the legal arguments raised and which affects the termination decision; and (4) bases for the default termination decision.

I. PROCUREMENT HISTORY

In 1991, EG&G Idaho, Inc. (EG&G), DOE's Management and Operating (M&O) contractor for the Idaho National Engineering and Environmental Laboratory (INEEL), began a procurement process, the object of which was to remediate radioactive waste and soil buried in the Subsurface Disposal Area which was part of the INEEL. The procurement activity was in response to initiatives from private industry, including LMAES. The area chosen was Pit 9, which was a repository of radioactive waste generated at the Rocky Flats Nuclear Weapons Facility located near Denver, Colorado, as well as INEEL waste.

It had been represented to DOE and EG&G that technologies existed within the private sector that were capable of successfully remediating the contents of Pit 9. One of the procurement objectives was to accomplish the remediation by the utilization of commercial technologies and management practices. In order to facilitate maximum input from private industry, the request for proposal (RFP) was first issued in draft form to a large number of firms. After receiving comments from industry, EG&G issued the RFP in final form in November 1991.

The RFP contemplated that the remediation effort would be conducted in three phases: Phase I, Proof-of-Process Demonstration Test; Phase II, Limited Production Demonstration Test; and Phase III, Full Scale Operation. The RFP made it clear that the subcontract type to be utilized would be firm fixed unit price, where the selected subcontractor was to design, install, operate, decontaminate and then decommission the remediation facility and be paid for its efforts on the basis of unit prices for soil and waste processed.

Three companies submitted proposals in response to the RFP of which none took exception to the subcontract type. Two firms, LMAES and Waste Management Environmental Systems (WMES), were deemed technically acceptable.

Based on questions raised by the Source Evaluation Board (SEB), and the fact that the rated technical scores of LMAES and WMES were essentially equal, EG&G and DOE decided to conduct an expanded Proof-of-Process (POP) test. The purpose of the expanded POP test was for each firm to prove to EG&G and DOE that elements of their respective processes

would, in fact, work as advertised. It was agreed that each firm would be paid \$8,000,000 for this effort and subcontracts for the performance of the expanded POP tests were entered into in November 1992 with results due one year later.

Towards conclusion of the POP test effort, in November 1993, EG&G decided that each firm would be given a change order to its POP test subcontract to produce a 30 percent design and draft Preliminary Safety Analysis Report (PSAR), based on their respective processes. EG&G, at the urging of the competing subcontractors, wanted to maintain the subcontractors' work force and schedule integrity during the time necessary for final selection. Both firms accepted the change orders and were paid approximately \$3,500,000 each to produce a 30 percent design and draft PSAR.

From April to early June 1994, there was significant written and oral dialogue between EG&G personnel and each of the competitors. All activities were brought to a close on July 12, 1994, when Best and Final Offers (BAFO) were received from LMAES and Rust Federal Services, Inc. (formerly WMES). LMAES was selected for award and a letter subcontract was executed by EG&G and LMAES in August 1994. A final definitized subcontract was issued on October 18, 1994, in the amount of \$178,600,000.

This procurement history is revealing in light of the assertions now being made by LMAES. LMAES was involved in the procurement process from the outset. LMAES had the opportunity for input into the RFP, defined and devised the POP tests to be performed with respect to its proposed technologies, performed those tests, reported success and were paid \$8,000,000 for its efforts. LMAES was then paid \$3,500,000 for the production of a 30 percent design and draft PSAR. For LMAES now to assert that it and/or EG&G lacked sufficient information to enter into a valid firm fixed unit price subcontract is disingenuous and does not comport with the facts nor with the contemporaneous documents.

In its BAFO, LMAES made it clear that it was well aware of both the nature of its contractual undertaking and the associated risks. The BAFO states, in the Overview: "Lockheed Environmental Systems and Technologies is pleased to submit this firm fixed price BAFO proposal. . . ." In response to several addenda issued shortly before BAFO, LMAES noted in its letter forwarding its formal price proposal:

. . . These revised requirements increased the risk associated with the project and increased the basic cost of the remediation effort. . . . Instead of increasing the Proposal price, . . . Lockheed hereby submits a Best and Final price . . . which is accounted for through an overall reduction of Lockheed's profit. This price includes the cost of technical

changes . . . , the additional programmatic risk associated with these changes and the risk to corporate assets associated with the acceptance of the Corporate Guarantee of Performance.

The BAFO then noted: "Lockheed takes no exception to the terms and conditions of this contract." Those terms and conditions include Clause 53, "Termination for Default (Revised)" of the EG&G Idaho, Inc. Standard Terms and Conditions for Purchase Orders and Subcontracts, Revised for Pit 9; June 1994 and Clause 6, "Termination for Default--Damages for Delay--Time Extensions" of the EG&G Idaho Inc. Construction Subcontract General Provisions, Revised for Pit 9; June 1994. Both of those clauses provide the authority for the contractual action which LMITCO is now taking.

II. REASONS NECESSITATING ISSUANCE OF THE CURE NOTICE

Having been provided funding for the production of a 30 percent design and draft PSAR, LMAES' BAFO incorporated a detailed technical proposal which provided a description of both the retrieval and remediation processes LMAES intended to provide, as well as the structures to house both. On its face, LMAES' BAFO represented a full and complete understanding of the technical requirements of the subcontract, as well as a commitment to perform its requirements. Schematic process and block flow diagrams were included with the BAFO, along with proposed equipment layouts. LMAES' BAFO proclaimed not only the "robust" nature of its process, but also its ability to exceed the performance requirements of the subcontract.

Unfortunately, LMAES' performance of its subcontract obligations has not been in accordance with the statements in its BAFO. A chronological history of some of LMAES' problems and the attempts LMITCO made to support project success are presented below.

- In October 1994, LMAES submitted a draft Systems Requirements Document (SRD) in accordance with the terms of the subcontract. Because of the many deficiencies in the SRD, there were numerous comments provided to LMAES as a result of LMITCO's review that required resolution by LMAES. LMITCO did not receive another SRD submittal until January 1997, 25 months after the comments were provided.³

³ This fact, omitted from LMAES' response, is particularly telling in light of LMAES' complaints about a "failure to agree upon a technical baseline." By definition, the SRD establishes a project's technical baseline. The "failure" was a failure by LMAES, not LMITCO or DOE.

- Just one month after award of the subcontract, in November 1994, LMAES announced its intent to delete the counter current ion exchange (CCIX) from the chemical treatment system. The CCIX was part of LMAES' POP test. The system performance impact is unknown, but the rather immediate departure from the technical proposal is indicative of a failure to maintain the technical baseline.
- In February 1995, LMAES submitted a draft PSAR that could not be approved due to the incomplete nature of the document.
- In May 1995, in a presentation to the Lockheed "Gold Team," LMAES announced that its original construction plan of multiple contracts would not support the scheduled completion date or cost. LMAES proposed obtaining a single general contractor for construction and installation. This was a significant shift in LMAES' project approach.
- In June 1995, LMAES was originally scheduled to have the chemical treatment system test bed construction and checkout completed. That milestone was never accomplished.
- In July 1995, LMAES replaced Merrick with Kiewit Construction Company as the Pit 9 construction manager. Merrick retained design responsibilities. This action is contrary to best management practices where, in a fast track environment, the designer is typically the construction manager as well.
- In September 1995, LMAES presented an informal schedule indicating a slip of two to three months in start of the Limited Production Test (LPT), a subcontract delivery date.
- In November 1995, LMAES advised that the overall schedule had slipped by 4.5 months.
- In March 1996, LMAES stated that it was probable that the schedule would be missed by approximately 10 months. LMAES declined to commit to a firm schedule.

- In April 1996, LMAES informed LMITCO that, as a result of significant concerns with the chemical treatment system (CTS), that system was being replaced with a soil sorter system. This represented a significant departure from LMAES' initial technical proposal. Reasons given by LMAES for abandonment of the CTS included large cost overruns, technical engineering problems, operational safety concerns, schedule delays, input materials variability, and the fact that LMAES' designer (Merrick) had not properly taken into consideration the maintenance and operability problems arising from the fact that the system was to be operated in a radioactively contaminated environment.⁴
- Lack of fire engineering involvement in initial design work resulted in design modifications and extensive field rework.
- In July 1996, LMITCO expressed concern about the ability of the soil sorter system to meet the subcontract requirement for volume reduction.
- In August 1996, LMITCO, based on LMAES' assertions of a new dedication to subcontract performance, issued a letter of forbearance with regard to the August, 15, 1996, subcontract start date for LPT. Concurrently, LMITCO demanded that LMAES submit a new schedule and plan for subcontract performance.
- In October 1996, LMAES submitted a proposed "path forward" formally substituting a soil sorter for the CTS. LMAES admitted the soil sorter would not achieve the 90 percent volume reduction required under the subcontract.⁵
- It should also be noted that, since the execution of this subcontract, until approximately October 1996, LMAES experienced significant turnover in key personnel. For example, LMAES had a total of four different Project Managers

⁴ This was confirmed by LMC's subsequently established Independent Cost Estimating ("ICE") team, which issued its report in 1996. The ICE team noted:

Merrick, the chosen A-E design agency, must not have understood the operational environment at the pit, including radiation protection and chemical protection and the conservative approach to criticality as well as ALARA. If they had understanding of the difficulties, they would not have designed this system the way it is configured. The chemical leach system is not maintainable in a rad environment, as an example. (Emphasis added.)

⁵ The ICE team later confirmed that substitution of the soil sorter for the CTS would require a subcontract modification as to the requirement for 90 percent volume reduction.

and eight different Contract Managers/Administrators. Certainly, this type of turnover was inefficient and had a negative influence on LMAES' ability to effectively manage the project.

From October 1996 through March 1997, LMITCO, together with DOE, the Environmental Protection Agency and the State of Idaho-Department of Environmental Quality, worked diligently with LMAES to enable it to define an acceptable path forward. Numerous meetings and conversations between the parties were conducted in support of that endeavor.

However, on March 28, 1997, LMAES submitted a Request for Equitable Adjustment (REA) which demanded: (1) a payment of \$127,800,000 for costs incurred by LMAES through March 31, 1997; (2) that the existing subcontract be reformed from a fixed price basis to cost reimbursement along with a 26-month schedule extension; and (3) "interim funding" of \$10,100,000 per month "during negotiations." In addition, LMAES failed to provide an estimate for cost to complete.

Rather than providing any cost analysis for costs incurred to date, LMAES stated that it had priced the REA on a modified total cost basis, essentially purporting to place all the responsibility for LMAES' claimed cost overruns (with the exception of approximately \$8,000,000 for the cost of seismic upgrades, scheduling costs, and increased G&A) on LMITCO and DOE.⁶

Meetings between LMITCO and LMAES were held in April and May 1997, to discuss various aspects of LMAES' REA. On May 7, 1997, LMITCO issued Modification No. 20 to the subcontract, which established a new schedule for performance. Modification No. 20 was based on schedule information provided by LMAES in connection with the REA. The revised schedule

⁶ The modified total cost approach would have placed almost all of the responsibility for the cost overruns on LMITCO. By contrast, the ICE Team Report (which was in LMAES' possession at the time the REA was submitted) placed primary responsibility on LMAES' lack of internal management:

Lack of Systems Engineering/Integration--The non-compliances to the specification and the ability of the subsystems to work together to form a totally compliant system are very obvious. While a Systems Engineering Management Plan was prepared and issued, there is inadequate evidence of effective implementation. . . . Systems Engineers possess a special skill and should not be created from another cloth, they do exist and should be used to do the requirements, design basis, contract language, verification and test program for effective project management. . . . Assigning a very high technology project to a Service Company will not usually result in a successful venture. This cleanup activity had and has the need for many highly specifically skilled individuals including: criticality engineers, robotics, physics of measuring radiation in a highly attenuated environment, and many more difficult skills. (Emphasis added)

extended the time for start of LPT to August 21, 1998, over two years after the originally scheduled start date. LMITCO determined the revised schedule was reasonable, as it (1) almost doubled the original time for performance, (2) was based on LMAES' own schedule information, and (3) was within LMAES' capabilities.

On May 14, 1997, LMITCO rejected LMAES' request for interim funding and subcontract restructuring. LMITCO indicated that the REA would be properly evaluated on its merits, but LMITCO was skeptical of the factual and legal bases for LMAES' claims, as well as the bases for LMAES' modified total cost pricing. Nevertheless, the Defense Contract Audit Agency was asked by LMITCO to review LMAES' cost and pricing records to determine if there was a sufficient basis for LMAES' REA claim.

LMAES responded by letter dated May 22, 1997. Although the subcontract changes and disputes clauses required LMAES to proceed, LMAES announced that it would “. . . consider a number of actions . . .” which included suspending ordering critical equipment, directing its subcontractors to slow down, and providing selected employees with notice under the Worker Adjustment and Retraining Notification Act. These actions were later reaffirmed in LMAES' letter of June 27, 1997, and implementation began on June 30, 1997. These actions severely impacted the design and construction of several of LMAES' major subsystems. LMAES' response to the actions taken by LMITCO on May 14, 1997, (i.e., rejection of interim funding and subcontract restructuring) was inconsistent with the subcontract terms and conditions requiring LMAES to proceed with performance of the subcontract.

In an attempt to justify its actions, on June 5, 1997, LMAES issued a letter which set forth 16 technical issues for which LMAES asserted it needed direction before it could continue with subcontract performance. Ironically, the majority of these issues had been identified by LMITCO in a February 24, 1997, letter to LMAES as issues which LMAES needed to resolve. The February 24, 1997, letter was a good faith attempt by LMITCO to establish a framework for reconciling those technical issues and to assure that LMAES would be able to fulfill its obligations with respect to design and safety requirements.

LMAES' June 5, 1997, letters specifically referenced its May 22, 1997, letter to LMITCO which conditioned LMAES' willingness to proceed fully with subcontract performance on both cost/schedule relief and technical direction. The June 5, 1997, letter set forth LMAES' interpretation of the subcontract requirements for 16 technical issues and stated that if LMITCO did not agree, “. . . this should be confirmed through the issuance of a formal change order . . .” The two letters taken together show that LMAES conditioned its full subcontract performance on LMITCO/DOE agreeing with LMAES' interpretations or on the issuance of change order.

Imposing these conditions was contrary to the subcontract requirements. The subcontract requires LMAES to fully proceed with the work while seeking relief under applicable subcontract provisions, even if LMAES disagreed with LMITCO's interpretation.

Despite the inappropriate form of LMAES' request, LMITCO undertook a good faith analysis of each issue. LMITCO responded on July 10, 1997, and pointed out that for each technical issue the answer could be found in either LMAES' BAFO or specific subcontract provisions or DOE orders that were referenced in the subcontract.

Instead of accepting the proffered direction, on July 25, 1997, LMAES responded with a letter challenging the adequacy of the direction. The deficiencies in direction which LMAES claims prevent it from proceeding pertain to parameters which are dependent on LMAES' system choices. These choices were intentionally not dictated in the subcontract so that LMAES would have the flexibility it needs to design systems and select subsystems that best suit its chosen processes. The July 25, 1997, letter indicated that LMAES did in fact understand the technical direction which it had been provided, but still did not proceed. LMITCO undertook yet another comprehensive review of the issues to determine whether the earlier direction had been clear and correct. On August 26, 1997, LMITCO responded and advised LMAES that the direction previously given was adequate and also directed that LMAES resume full-scale operations. LMAES disputed this in its letters of August 29, September 15, and October 29, 1997. LMITCO, for the third time, undertook a detailed analysis of the issues and provided that analysis to LMAES on November 26, 1997. This letter also concluded that previously provided technical direction had been adequate and further directed LMAES to return to work.

On February 6, 1998, LMITCO received a letter in which LMAES continued to challenge not only the adequacy of the direction, but now maintained that proceeding with the subcontract required LMITCO's prior agreement to LMAES' technical baseline as well as an agreement on a subcontract pricing modification. Neither demand is consistent with the subcontract. If LMAES felt the technical direction given by LMITCO was a change to the subcontract, LMAES' recourse, pursuant to the changes and disputes clauses, was to proceed as directed while submitting a properly documented REA for any alleged changes. Unfortunately, it appears that LMAES is unwilling to accept the fact that there is no contractual basis that compels LMITCO to grant advance approval of design configuration, additional funding, and subcontract restructuring. LMAES chose to stop work for reasons known only to it, but it cannot attribute work cessation to a lack of technical direction.

These and other examples of LMAES' intransigence have been discussed in numerous letters, meetings, and telephone conversations between LMITCO and LMAES personnel. Unfortunately, despite the fact that LMITCO has repeatedly directed LMAES to return to work, LMAES has never complied with that direction. LMAES reiterated in letters dated March 28, July 11, July 25, August 29, and October 29, 1997, that it would not resume operations unless LMITCO changed previously given technical direction, altered the subcontract pricing structure, provided interim funding, instituted a new schedule and reduced the performance parameters.

Since July 1997, LMAES has only performed a number of minor activities such as: (1) the initial melter Factory Acceptance Testing was performed at Retech in Ukiah, California, and the punch list items were identified and corrected (further testing remains); (2) Parsons continued limited design effort on the CTS; and (3) some installation of fiber optic cables in the Retrieval building has been performed. A comparison to the current subcontract schedule indicates that these activities and the claimed "major engineering achievements/activities" set forth in the response to the cure notice are not substantive in light of all the other things that are not happening. While continuing to maintain in writing that LMAES stands ready to perform, LMAES' actions (such as actually laying off almost all of its employees in August 1997, and interrupting performance by its subcontractors and suppliers) have been and continue to be exactly contrary. LMAES has fallen so far behind schedule that it is virtually impossible to meet its subcontract obligations.

The conditions imposed by LMAES for restart were untenable; therefore, LMITCO had no alternative but to issue a cure notice, which it did on February 27, 1998.

III. EXCUSES FOR NONPERFORMANCE

LMAES categorizes its excuses as follows:

- “(1) DOE’s material pre-award misrepresentations with respect to Pit 9 contents;
- (2) DOE’s post-award refusal to cooperate with LMAES in a good faith effort to define the subcontract requirements; and
- (3) DOE’s unwarranted interference in the administration of the Pit 9 Subcontract.”

As stated at the outset of this letter, this is not the appropriate place to provide a detailed response to each of the myriad excuses advanced by LMAES for nonperformance. Suffice it to say that LMITCO has carefully considered the legal arguments made by LMAES in the April 13, 1998, response, in light of the facts and circumstances of this subcontract, and has found

LMAES' excuses presented to be unsubstantiated and unpersuasive. There is, however, one matter that needs to be addressed: LMC's argument with regard to the organizational conflict of interest (OCI) between LMITCO and LMAES, which is said to prevent a default action by LMITCO.

It should be pointed out that this OCI issue was first raised by LMC's letter of March 6, 1998. Similar but expanded assertions are contained in the April 13, 1998 response to the cure notice. It does not appear that LMC's March 6, 1998, letter and the response to the cure notice raised the OCI issue because of LMAES' concern that LMITCO will act contrary to the interests of the United States Government. Rather, the actions suggested in the letters to prevent LMITCO from issuing a default termination would not serve to protect the interest of the Government as the M&O contract requires. In fact, these actions could be interpreted as serving exclusively to protect the interest of LMC at the expense of the Government. There is an incongruity between insistence that there are unmitigatable conflicts of interest when a default action looms and the failure to identify these issues when accepting payment for work performed under the subcontract and the prime contract.

Parallel to the solicitation for the Pit 9 subcontract, DOE had been conducting a solicitation for the award of a new M&O contract at the INEEL. LMITCO was one of the competitors. In the summer of 1994, DOE selected LMITCO as the new M&O contractor. Although both LMAES and LMITCO are separate corporations, they are both wholly owned subsidiaries of LMC. The DOE contracting officer prudently concluded that it would be a conflict of interest and personally uncomfortable for the M&O contractor employees to negotiate with LMAES over the price and final terms of the subcontract. For these reasons and at EG&G's request, the DOE contracting officer assumed responsibility for the subcontract and negotiated a price of \$178,600,000. When LMITCO began performing the M&O contract, its act in awarding the \$178,600,000 subcontract to LMAES was only to definitized a letter subcontract which had already been awarded by a totally separate contractor, at a price that had been negotiated under the auspices of DOE. Despite these safeguards, the DOE contracting officer recognized that having LMITCO administer a subcontract awarded to an affiliate would raise OCI issues.

In addition to negotiating the subcontract price and final terms with LMAES, the DOE contracting officer negotiated a series of internal and external controls with respect to the LMITCO/LMAES relationship. LMITCO's M&O contract includes Clause I.63, "Organizational Conflicts of Interest--Special Clause." That special clause contains a specifically tailored subparagraph by which LMITCO's organizational conflicts of interest affirmative compliance plan had been approved by DOE and included in the contract. That plan mandated that LMITCO personnel make decisions that are impartial with regard to self interest. The plan further added

that "Lockheed Idaho is committed to conducting its business in a manner that is in the best interest of the government and the Department of Energy." It further states: "It is not the intent or purpose of Lockheed Idaho to benefit its affiliates (including Lockheed Corporation and its subsidiaries and divisions) beyond the normal flow of benefits from performance of this contract." LMITCO and LMC consciously and unqualifiedly accepted all of these requirements.

Despite these protections, the DOE contracting officer was still reluctant to have LMITCO administer LMAES' subcontract. He acquiesced only after LMITCO's president steadfastly and unqualifiedly urged that excluding this important subcontract would impair the effectiveness of the M&O. To allay DOE concerns, LMITCO submitted a specific OCI plan for Pit 9 and vouched for its effectiveness. Contrary to LMC's March 6 letter, and the response to the cure notice, this plan was not unilaterally imposed by DOE; it was drafted and urged by LMITCO to address the concerns of a reluctant DOE contracting officer. And, more to the point, it is undisputed that the plan was executed by both LMITCO and DOE.

The argument with regard to the termination decision is not well taken. The authority to terminate has been specifically provided for in the LMAES subcontract since formation. Article 1, "Definitions," of the Subcontract, in subparagraph (d) states that: "The term 'contractor' means Lockheed Idaho Technologies Company or any duly authorized representative thereof." Article 8 of the subcontract, "Contractor's Administration," states that: "Unless the subcontractor is otherwise notified in writing, the contractor's responsibility under the subcontract shall be administered by Gary H. Longhurst, Subcontract Administrator . . ." On January 24, 1995, LMITCO sent to LMAES GHL-09-95, titled "Delineation of Delegated Authority." That letter reaffirmed Article 8 and added:

"At present, LITCO personnel having the authority to direct LESAT in the performance of their work under Subcontract No. C91-133136 are Gary H. Longhurst (Subcontract Administrator), Steve L. Lewis (backup Subcontract Administrator), and P. James Simonds (Manager, Subcontract Administration). The LITCO personnel identified above, or others further identified in writing at a later time, are the only ones authorized under the subcontract to act for and on behalf of LITCO in their designated capacities."

LMAES has never objected to Article 8 nor the January 24, 1995, letter. Indeed, it has accepted direction, change orders and modifications signed by the subcontract administrator. There is simply no basis for now saying that because a termination decision will have adverse financial consequences to LMC and LMAES, that decision is different in kind than all of the other decisions made by the subcontract administrator under an OCI plan which LMITCO actively sought and, indeed, authored.

IV. BASES FOR DEFAULT

A. FAILURE TO MAKE PROGRESS

LMAES' actions--laying off virtually all of its employees; stopping all meaningful efforts by its subcontractors and suppliers; and refusing to perform unless LMITCO accedes to its demands on technical matters or promises change orders for matters which are not changes--have resulted in a failure to make progress so as to endanger performance of the subcontract. Despite LMITCO's reasonable request for adequate assurances, LMAES has refused to give such assurances or even to evince any inclination or obligation to make progress on this subcontract.

B. LMAES HAS REPUDIATED ITS SUBCONTRACT OBLIGATIONS

The March 6, 1998, letter from LMC to DOE, contains the following statement:

“LMAES' obligation to perform the Pit 9 subcontract terminated on September 13, 1997 . . . Lockheed Martin is not required to continue to attempt to remediate Pit 9.”

This statement and the logic behind it had never before been presented by LMAES or any LMC official. It is difficult to conceive a more clear example of a repudiation of the subcontract. The essence of a contract is that both parties are obligated to perform. LMC's letter of March 6, 1998, clearly and unequivocally states that LMAES is not so obligated to continue to perform and indeed has not been so obligated since September 13, 1997. Consequently, whatever meager efforts at performance that LMAES has claimed were ongoing or that LMAES professes will occur in the future are not the result of any perceived contractual obligations, but are merely voluntary acts by LMAES and therefore stoppable whenever LMAES decides to do so.

Performance at the sole discretion of one of the contracting parties is not performance of a contract. Therefore, statements in LMC's March 6 letter clearly indicates that LMAES does not consider itself bound by the Pit 9 subcontract, nor does it intend to perform in accordance with the Pit 9 subcontract which it views as having ended eight months ago. LMAES has clearly repudiated its obligations under the subcontract.

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V. CONCLUSION

Subcontract No. C91-133136 and LMAES' right to proceed under it is hereby terminated for default. This termination for default is for: (1) failure to make progress so as to endanger performance; and (2) LMAES' repudiation of its obligations under the subcontract. LMITCO has determined that LMAES' failures are not excusable as explained above, and LMAES is in default. LMITCO reserves all rights and remedies provided by law or under the subcontract including charging LMAES with appropriate excess costs of reprocurement. LMAES has the right to dispute this decision under the disputes clauses of the subcontract.

Pursuant to Article 14, Guarantee of Performance, of the subcontract, you are hereby directed to return to LMITCO the sum of \$54,386,165 within 30 days after receipt of this letter.

Sincerely,

Gary H. Longhurst
Senior Subcontract Administrator

cc: D. P. Letendre, DOE-ID, MS 1221
J. F. Nagle, Esq., Oles Morrison and Rinker
P. B. Teets, Chief Operating Officer, LMC (by Certified Mail)
F. G. Schwartz, DOE-ID, MS 1117

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bcc: S. O. Baldwin, MS 3402 (Project Files)
C. N. Fitch, MS 3402
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P. J. Simonds, MS 3521
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ER ARDC Pit 9 File, MS 3922
G. H. Longhurst File (GHL-031-98)